Causes of the Great Depression

World History 3201
2.2.5: Using historical documents to explain how each of the following factors was a major cause of the Great Depression: (a)

- over-production and over-expansion by businesses
- consumer overspending with credit during the Roaring Twenties
- impact of high tariffs on international trade
- too many purchases of stocks on credit
Unit Overview

- World-wide economic downturn from 1929-1939
- Began with the crash of the stock market on October 29, 1929 (Black Tuesday)
- Dirty Thirties
- Breadlines, Relief Camps, Unemployment
- Emergence of the Welfare State
- Emergence of new political parties (left wing)
- WWII helped economic growth
• After the boom years of the 1920s, a dramatic economic shift in 1929 would change the world economy & society

• The good times of the 1920s abruptly ended not just in America but in most industrialized countries

• In order to understand the Great Depression, we must first briefly look at the business cycle & develop a basic understanding of the stock market
Economic conditions constantly change, in other words there are good time and bad times, economists call these upswings and down swings the **business cycle**.

There are four basic stages to the cycle:

- Recovery (Expansion)
- Prosperity (Boom)
- Recession
- Depression (Trough)
The Business Cycle

1919-1923
- Declining: sales, wages, prices, production, business profits, demand for goods
- Increasing: Business failures, unemployment
- High: Labour Unrest (many strikes)

1923-1929
- Increasing / high sales, wages, prices, production, business profits, demand for goods,
- Decreasing / low unemployment & business failures

1929-39
- Low: sales, wages, prices, production, business profits, demand for goods, labour unrest (few strikes)
- High: Business failures, unemployment

Recession
Depression
Expansion
Boom
Recession
Depression
How the Stock Market Works

- The boomtime of the 1920s created such confidence in the economy that many people bought stocks in businesses
- Stocks: shares in a company that can be bought & sold
- Stock market: a place where businesses raise money by selling stocks, or shares, in their business
How The Stock Market Works

The owners of Nova Manufacturing Company want to sell stock in the company to raise money for expansion.

Mrs. Jones has some money and she would like to use it to make some more money. She buys shares in Nova, hoping their price will go up.

Stockbrockers, or salespersons, meet here to buy and sell stocks for clients like Mrs. Jones.
The Stock Market

- During the 1920s, a stock market **boom** developed as the price of stocks increased in value.
- It was a relatively easy method for becoming wealthy.
- In 1929 investors were very confident that stocks would remain high despite some notable economic problems.
- By September, American stock market shares began to drop & American stock values followed.
Worried investors began to **lose confidence** in the companies whose shares they had purchased & many wanted to **sell** their stocks quickly before prices decreased any further.

As investors began selling large volumes of stock, people panicked & tried to sell their stocks, the values of which fell dramatically.

By Tuesday October 29th, the stock exchanges in New York, & around the world “**crashed**”
Impacts of the “Crash”

- Many investors were financially ruined left with stocks that were worth a fraction of their earlier values.
- Many had bought stocks on margin (10% down payment) or with borrowed money & were unable to sell their stocks to pay their debts.
- While only a small % of Americans owned stocks, millions of Americans were affected by the crash of 1929, the first visible evidence of a worldwide economic collapse that became known as the Great Depression.
Great Depression: Underlying Causes

- While the 1929 stock market crash served as a catalyst of the Depression, there were underlying contributing factors. These included:
  - Over-production & over expansion of business
  - Purchasing stock/buying on margin
  - Purchasing on credit/high consumer debt
  - High tariffs/limited trading partners/ protectionism
During the prosperous 1920s, agriculture & industry reached high levels of production.

Almost every industry was expanding which meant that huge supplies of food, newsprint, minerals, & manufactured goods were produced & simply stockpiled.

The was an over supply while demand was low. For example: 1930 over 400 000 cars produced while 260 000 was the most cars sold in a year.
Over Production

- Industrialists seemed to have forgotten a basic lesson in economics: **produce only as many items as you can sell**
- Even in the general prosperity of the 1920s, Americans could afford to buy only so many goods
- As a result, warehouses became full of unsold goods, soon the factory owners slowed down production & laid off workers
- The laid off workers & their families had even less money to spend on goods which slowed sales even more.
For many people during the 1920s, the stock market seemed an easy way to get rich quickly with relatively little money.

At that time you could *buy stocks on credit* just as you could a washing machine or phonograph.

For only a 10% down payment, a stockbroker loaned you the rest of the money at a high rate of interest.

To buy $1000 worth of stock you needed only $100.

As soon as your stocks went up in value, you could sell them, pay back your broker, & pocket the profit.
The idea was that as soon as your stocks went up in value, you could sell them, pay back your broker, & pocket the profit.

This risky process was called “buying on margin.”

What if the stocks didn’t go up? Or, worse still, what if they went down?

You would have to sell your stocks or face financial ruin.
This is exactly what happened in October 1920
When stock prices started to fall, people panicked, decided to sell and get out of the market
Prices fell even lower as more and more stocks were dumped
On **Black Tuesday, October 29, 1929**
stocks decreased by 50%
Shareholders lost millions & many big and small investors were wiped out in a few hours
Throughout the 1920s, Americans were encouraged by advertising to "buy now, pay later".

Why wait to buy a washing machine or automobile when you could have it immediately with a small downpayment?

Many families got themselves hopelessly into debt with credit buying.
The piano that cost $445 cash was purchased with $15 down & $12 a month for the next four or five yrs

With interest payments, it ended up costing far more than it was worth (many purchases ready for junk pile when paid off)

If sickness or layoff occurred, making payments could be difficult

Repossession of homes, cars, appliances would occur when payments could not be met
Terrible drought of 1921, 1931, 1933-1937 reduced production of wheat
Farmers cant afford their mortgages, railways and flour mills slow down.
Chain reaction to all parts of the economy
Tariffs are taxes on foreign goods. Using high tariffs to keep out foreign goods is called protectionism. Every country attempted to save its own industries by trying to ensure that they did not face tough competition from foreign industries. As a result, industries in other countries suddenly found their usual overseas markets closed off.
Countries with high tariffs that practiced protectionism strangled international trade as country after country shut its doors to goods from abroad.